United States Court of Appeals

for the Second Circuit

BRIEF FOR APPELLANT

76-7068

To be argued by
JOSEPH LOTTERMAN

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P/S

United States Court of Appeals

FOR THE SECOND CIRCUIT

INTERNATIONAL HALLIWELL MINES, LIMITED and LA SOCIETE D'EXPLOITATION ET DE DEVELOPPEMENT ECONOMIQUE ET NATURAL D'HAITI,

Plaintiffs-Appellants,

—against—

CONTINENTAL COPPER & STEEL INDUSTRIES, INC., MORTIMOR S. GORDON, MIDLANTIC NATIONAL BANK, as Executor of the Estate of WALTER H. KNORR, SAMUEL M. GOLDMAN and DELIA JACOBS, as Executors of Estate of SAMUEL UNGERLEIDER, MARION V. WHEELER, as Executrix of the Estate of ARTHUR WHEELER and ELEOS HARRIS, ROBERT HARRIS and JOSEPH STEINHARDT, as Executors of the Estate of HARRY HARRIS,

Defendants-Appellees.

BRIEF OF PLAINTIFFS-APPELLANTS INTERNATIONAL HALLIWELL MINES, LIMITED AND LA SOCIETE D'EXPLOITATION ET DE DEVELOPPEMENT ET NATURAL D'HAITI

LOTTERMAN & O'CALLAGHAN
Attorneys for the Plaintiffs-Appellants
103 Park Avenue
New York, New York 10017
683-8281

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The Nature of This Appeal

Plaintiff-Appellant INTERNATIONAL HALLIWELL MINES, LIMITED ("Halliwell"), a publicly held Canadian Corporation, and its wholly owned subsidiary, the plaintiff-appellant, LA SOCIETE D'EXPLOITATION ET DE DEVELOPPEMENT ECONOMIQUE ET NATURAL D'HAITI ("Sedren"), a Haitian corporation which owned a copper mine in Haiti under a 25 year concession from the Haitian government, appeal from a judgment of Judge Dudley B. Bonsal, dated January 26, 1976 and duly entered on January 27, 1976, dismiss-

ing the amended complaint of the plaintiffs with prejudice and upon the merits. (57a-59a)*

The Proceedings in the Court Below

(1) The Plaintiffs' Amended Complaint (6a-19a)

It is alleged in the amended complaint, that Halliwell-Sedren, during the relevant periods specified therein, were wholly dominated and controlled by the defendant Continental Copper & Steel Industries, Inc. ("Continental") and the individual defendants, all of whom were officers and directors of Continental while they were serving as directors of Halliwell-Sedren.

It is further alleged that Continental exacted its several contracts with Halliwell-Sedren** for the benefit of Continental and to the enormous prejudice of Halliwell-Sedren; appropriated the corporate opportunities of Halliwell-Sedren for the exclusive benefit of Continental; and reaped unconscionable profits from that domination and control at the expense of Halliwell-Sedren, in complete violation of the fiduciary duties and obligations which the individual defendants and Continental owed to Halliwell-Sedren and their stockholders. As a result of the defendants' actions, Halliwell-Sedren were destroyed as viable corporate and commercial enterprises. The Sedren mining concession was eventually terminated and cancelled by the Haitian government.

On April 12, 1967 the individual defendants, *then consisting of five of the eight members of the Halliwell*

* Unless otherwise indicated, all page references with the suffix "a" are to the Joint Appendix. All page references with the suffix "A" are to the Exhibit Volume.

** Several contracts were executed by Continental and Sedren, with performance by Sedren being guaranteed by Halliwell. In our ensuing discussion, they will be considered as single contracts of Halliwell and Sedren.

*Board,** directed the execution of general releases to Continental by Halliwell and Sedren ("the April 1967 releases"). It is the position of the plaintiffs that those releases, under the By-Laws of Halliwell and the general rules of law applicable to fiduciaries who purport to absolve themselves of liability by releases *voted by themselves to themselves*, were totally void.

In addition, approximately one year later, an agreement dated March 15, 1968 (the "March 1968 agreement") was exacted by Continental from the plaintiffs under the appalling economic conditions in which the defendants' actions had left the plaintiffs. That agreement purported to terminate the prior contracts between Halliwell-Sedren and Continental, and ratify the previously executed releases. It was claimed by the defendants to effect a "settlement" of Continental's obligations, as well as the obligations of the individual defendants. In connection therewith, the plaintiffs established that, in March of 1968, they were completely helpless and were compelled by the economic *extremis* to which they had been reduced by the actions of the defendants in violation of their fiduciary obligations, to surrender to the terms of the agreement dictated by Continental and the individual defendants, with no other alternative available to them except total extinction.

(2) The Defendants' Answer (25a-32a)

By their answer, the defendants denied the material allegations of the amended complaint and set forth several affirmative defenses thereto, including, particularly, the defense of release predicated upon the April, 1967 general releases, and the defense of settlement predicated upon the March 15, 1968 contract (28a) Those defenses were interposed by both Continental and the individual defendants, all of whom, through the years that they served as direc-

* All italics are ours unless otherwise indicated.

tors of the plaintiffs, were the principal officers and directors of Continental.

It must be emphasized, at this point, that none of the individual defendants was named in the April 1967 releases; that none of the individual defendants was a party to the March 15, 1968 agreement; and that not a word is contained in either of these documents which purports, directly or indirectly, to absolve the individual defendants of the manner in which they utilized their positions as directors of the plaintiffs solely and only for the benefit of Continental.

(3) The Limited and Restricted Trial Before the Court

As appears from his opinion, Judge Bonsal, to whom the case had been transferred from Judge Owen under the so-called "Crash Program," ruled that he would "try the issues raised in the affirmative defenses as to the validity of the Settlement Agreement and of the releases given by Halliwell and Sedren, before considering the other issues raised in the amended complaint since, if the defendants prevailed it would be the end of the case". (37a-38a)

In its opinion (35a-56a), the District Court sustained those defenses and thereafter entered a judgment dismissing the amended complaint. (57a) The plaintiffs herein appeal from that judgment. (58a-59a)

The Issues Presented for Review

As a result of the District Court's decision, the defendant Continental and the *five individual defendants*, each of whom was a director or officer of Continental and all of whom were members of the Board of Directors of the Appellants Halliwell or Sedren, or both, *as the nominees of Continental* during the period of time involved in the action, *have been judicially permitted to exculpate themselves by their own acts*, from their liability for their ap-

propriation for the benefit of Continental of the assets, properties and corporate opportunities of the plaintiffs.

The District Court ruled that the *five Continental nominees* who, out of *a Board of eight*, voted for the execution of general releases from Halliwell-Sedren to Continental, by threatening the plaintiffs with insolvency unless the releases were executed, and thereafter procured an alleged ratification of those releases in a termination agreement between the plaintiffs and Continental under a like threat of insolvency, had successfully absolved Continental from liability and themselves as well, in spite of their violation of their fiduciary obligations to the plaintiffs and the fact that, both under the By-Laws of the plaintiffs and existing law, they were absolutely disqualified from constituting a quorum or voting at the meeting at which the releases were exacted and thereafter obtaining a reaffirmation of those releases under the grossest form of economic duress.

It is the position of the plaintiffs that the District Court erred in dismissing the plaintiffs' amended complaint under the facts established herein, thereby judicially sanctioning the unilateral action of the Continental nominees who served upon the Board of Directors of plaintiffs in exculpating Continental and themselves from liability for the breach of their fiduciary obligations to the plaintiffs and their stockholders, by voting general releases to Continental and procuring a ratification thereof from virtually bankrupt plaintiffs without any disclosure to, or the knowledge of, the plaintiffs' stockholders of Continental's depredations.

According to the District Court, those releases and the subsequent alleged ratification thereof likewise enured to the benefit of the individual defendants *as servants of Continental*, notwithstanding their activities as Halliwell directors in appropriating the assets and corporate opportunities of the plaintiffs for the benefit of Continental which ultimately resulted in the total insolvency of the plaintiffs.

Statement of the Case

The Parties

(1) The plaintiff Halliwell is a publicly held Canadian corporation. Through Sedren, its wholly-owned Haitian subsidiary, it owned and operated a copper mine in Haiti under a 25 year concession granted by the Government of Haiti. (Defts Ex. C, 252A-253A, 255A, ¶¶ 2, 3, 10)

(2) The defendant Continental is a Delaware corporation (Defts Ex. C, 253A, ¶ 4) whose principal business is, in the language of MORTIMOR S. GORDON ("Gordon"), its President and Chief Executive Officer, "the manufacture and sale of wire and cable". (Gordon, 7).* All of the individual defendants were directors and officers of Continental. (Defts Ex. C, 253A-255A) The defendant WALTER KNORR ("Knorr") was the Treasurer and a Vice-President of Continental; and the defendants HARRY HARRIS ("Harris"), SAMUEL UNGERLEIDER ("Ungerleider") and ARTHUR WHEELER ("Wheeler") were directors of Continental. During the relevant periods involved in the complaint, Messrs. Gordon, Knorr, Harris, Ungerleider and Wheeler were all directors of Halliwell and Sedren.** (Defts Ex. C, 253A-255A)

The names of two other companies will appear during our statement of the case: National Outlook Corporation ("National Outlook") and Consolidated Mogul Mines, Ltd. ("Mogul").

National Outlook is an investment company of which the defendants Gordon, Harris and Ungerleider, Directors of Continental, were likewise directors and stockholders.

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* The foregoing reference, as well as like references, are to the depositions of the persons named, and the pages thereof.

** In several passages of the District Court's opinion, there is an indication that the Continental nominees were four in number. (50a) From June 20, 1961 to July 25, 1967, the Continental nominees were always five in number.

Adolph H. Graetz ("Graetz"), a director and vice-president of Halliwell-Sedren, was also a director, officer and stockholder of National Outlook. (Graetz, pp. 3-4) National Outlook was interested in what Gordon called "special situations" (Gordon, 42), to wit unique circumstances which presented the possibility of substantial and profitable returns from investments or loans. It became a substantial holder of Halliwell debentures and common stock.

Mogul is a Canadian corporation engaged in the development of mines throughout the world, and had for sometime prior to January, 1959 provided financial assistance to Halliwell for the development of the Sedren mine. It was likewise a substantial owner of Halliwell debentures and common stock.

Statement of the Relevant Facts

Under this Court's decision in *First National Bank of Cincinnati* v. *Pepper*, 454 F.2d 626, in resolving the issues presented upon the limited trial herein, it was essential to determine the existing and antecedent circumstances under which both the releases of April 28, 1967 and the agreement of March 15, 1968 were executed. As this Court declared (p. 632):

> "In our view the district court was required to give consideration to *all of the facts* relied upon by the stockholders as evidence of duress rather than rely exclusively upon the terms of the compromise agreement and the pendency of the New York Supreme Court proceeding."

Notwithstanding the foregoing decision which was pressed upon the District Court by the plaintiff's counsel during the course of the trial (Tr. 44-51),* the Court below

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* All references to the pages of the trial transcript will be prefixed by the letters Tr.

severely and erroneously restricted the plaintiff's ability to submit to the Court, for its consideration, "all of the facts" relied upon by the plaintiff as evidence of invalidity and duress.

The most egregious of the errors committed by the Trial Court was its adamant and inexplicable refusal to permit plaintiffs to call Adolph Graetz as its principal witness (Tr. 40-51). Graetz, a Halliwell director from 1961 until long past 1968, was prepared to testify from his own personal knowledge, in the greatest detail, to the circumstances under which the 1964, 1967 and the March 15, 1968 contracts, as well as the 1967 general releases, were exacted from Halliwell-Sedren by Continental and the Continental nominees upon the Halliwell-Sedren Boards (Tr. 42; 44-45; 50; 53).

The District Court's incomprehensible refusal to allow Graetz to testify for the plaintiffs gravely handicapped the plaintiffs in establishing under this Court's decision in *Pepper*, supra, "all of the facts" relied upon by the plaintiffs as evidence of invalidity and duress. The Trial Court's awareness of the immense importance of Graetz's testimony to the plaintiffs' case, manifested by their counsel's continued insistence thereon in the extended colloquy with the Court, as well as his objections and exceptions to the Court's ruling, is reflected in the following statement by the Court to counsel (Tr. 50):

> "The Court: I know you say all that, but I will hear Bell shortly, but I am not going to hear this other gentleman (Graetz).
>
> You may think the Court of Appeals will reverse me, but that is all right, too."

The plaintiffs were, therefore, understandably startled to be told by the Court in its opinion that (52a):

> "In denying summary judgment, Judge Owen stated that 'there are questions of fact as to the degree of

> control and of possible duress exercised over plaintiff throughout the period relevant to this action.' Plaintiffs have now been afforded the opportunity to introduce evidence to prove possible duress and the full record is before the Court.

Since Graetz's affidavit was the only affidavit submitted by the plaintiffs to Judge Owen upon the motions for summary judgment, it is impossible to understand how, by the Trial Court's exclusion of Graetz as plaintiffs' witness, "the full record was before the Court" or how the "Plaintiffs have now been afforded the opportunity to introduce evidence to prove possible duress . . .".

I.

The Events Preceding the Execution of the 1964, 1967 and 1968 Continental-Halliwell-Sedren Agreements, and the April 1967 Releases.

(1) The Inception of the Relationship Between Continental and Halliwell

As appears from the minutes of the meeting of Continental's Board of Directors of January 22, 1959, Harris had approached Gordon prior to that date with a proposal involving Mogul and Halliwell. Halliwell had planned to construct a concentration and preparation plant for its Haitian mine which required the expenditure of several millions of dollars. Mogul which had provided Halliwell with certain financing prior to that date was now seeking to obtain "the required financing from other sources . . ." Gordon was interested in the proposal presented by Harris because it constituted an opportunity which would enable Continental *"to control a source of copper"*, a position which Gordon deemed important for Continental. (Gordon, 9-25; Pltffs Ex. 14 for Id., 159A-161A)

As appears from the Continental Board minutes of that day, the proposal was rejected by Continental's Finance Committee because, among other things, the Company "lacked experience and know-how in the mining business . . .". (Gordon, 25)

Thereafter, Continental continued its negotiations with Mogul and Halliwell, and explored the possible association in the venture of the Chase International Investment Corporation ("CIIC"), a wholly-owned subsidiary of the Chase National Bank ("Chase").

Prior to Gordon's communication with the Chase, he received a report prepared by W. W. Weber ("Weber"), Mogul's geologist, setting forth Weber's estimate of the amount of ore reserves at the Sedren mine (Gordon, pp. 16-17), a copy of which had been made available to the Chase (Gordon, p. 18). The Chase sent its own geologist, G. J. Krueger, to Haiti for the purpose of examining the mine. Gordon was advised by the Chase of the result of Krueger's trip (Gordon, p. 14), the substance of which was that "the ore reserves (of Weber) had been *grossly overstated*, that the property to be operated required considerable expertise" in the mining field (Gordon, pp. 15, 18). Thereafter, the Chase withdrew from the picture. (Gordon, p. 28)

(2) The Continental-Halliwell-Sedren Contract of April 1, 1959 (Defts Ex. D, 262A-268A)

The Continental-Halliwell-Sedren contract of April 1, 1959 was obtained by Continental from a necessitous Halliwell without the expenditure of a single penny by Continental in meeting Halliwell-Sedren's financial needs at the time. It was based upon the following mutually shared assumptions, hypotheses and estimates at the time, none of which were warranted as existent facts. Thus, there appears at the very outset of the contract, the following recitals (Defts Ex. D, 263A):

(1) That "Sedren *is now proceeding* to erect a plant for the mining and concentrating at a minimum rate of 1,500 tons per day of copper ores from the Terra Neuve area of the concession granted by the Government of Haiti to Sedren";

(2) That "it is *anticipated* that production of concentrates from treating said ores will commence in or about the month of September, 1960"; and

(3) That "Sedren has *estimated that 80,000,000 pounds of copper are recoverable* from the ore reserves established in said concession and *can be produced therefrom by June 30, 1964.*"

The foregoing recitals underscore the speculative estimates and contingencies upon which the contract was based. On April 1, 1959, it was impossible to predict, with any degree of certainty, that the plant which Sedren was then proceeding to erect would be so wholly completed and smoothly functioning that the production of copper concentrates would unquestionably commence in or about the month of September, 1960. Moreover, to Gordon's knowledge, the estimated existence of 80,000,000 pounds of copper by Weber had been characterized by the Chase geologist as "grossly exaggerated", a characterization substantially confirmed by George Tower, Continental's mining expert. (Gordon, p. 126) Furthermore, the likelihood that 80,000,000 pounds of copper, even if it existed, could be produced from the Haitian ore reserves by *June 30, 1964* was extremely dubious. Finally, the copper which Halliwell and Sedren were required to deliver were not copper concentrates produced from the Sedren mine. It was, instead, "electrolytic copper in wire bars" which, concededly, Sedren had no ability to produce. (Gordon, p. 32)

Based upon, and obviously subject to, the accuracy of those estimates and assumptions as determined by the future, Halliwell-Sedren agreed in the April 1, 1959 contract with Continental:

(1) To sell to Continental the first 80,000,000 pounds of copper metal recovered by Sedren from copper concentrates produced by Sedren from the Haitian mine;

(2) To deliver that amount of copper "in wire bars";

(3) *To commence deliveries no later than the month of January, 1961*, at the rate of not less than 1,500,000 pounds per calendar month and not more than 3,000,000 pounds per calendar month.

In addition thereto, the contract provided for a discount to Continental at varying prices (Defts Ex. D, 264A), and in paragraph 7 for liquidated damages "Should Sedren fail to complete the delivery of the 80,000,000 pounds of copper . . . on or before June 30, 1964." (Defts Ex. D, 265A-266A)

It was further provided in paragraph 9 thereof that "this Agreement shall be construed in accordance with, and the rights of the parties shall be governed by, the laws of the State of New York." (Defts Ex. D, 267A)

By the execution of the April 1, 1959 contract, Gordon had taken a long step forward toward the fulfillment of his desire "to control a source of copper" and free Continental from its total dependence upon mine producers and the vagaries of the copper market. It was anticipated that the Sedren mine would alone furnish Continental with "a substantial part of its copper requirements", i.e., 25 to 33⅓ percent. (Gordon, p. 123)

Gordon thereupon embarked upon a source of action designed to achieve, ultimately, complete control of Halliwell's management, mine, operations and finances for the benefit of Continental. That goal was accomplished by June of 1961.

(3) The June 1961 Financing of Halliwell and Sedren

On May 2, 1961, as appears from the minutes of a meeting of the Halliwell Board held at Gordon's law office* (Tr. 20; Pltffs Ex. 16 for Id., 162A-166A), a financing arrangement was proposed by Gordon which he outlined as follows (164A):

> "1. The Company to increase its capital to 12,000,000 shares by creating 2,000,000 additional shares.
>
> 2. Continental to purchase 1,000,000 of the said shares at 40¢ U.S. per share which would provide $400,000 U.S. to the Company.
>
> 3. Mogul to purchase $132,000 principal amount of the Company's debentures at $96.00 per $100.00, the advances of $125,000 made by Mogul to the Company and interest accruing thereon to be credited against the purchase price of the said debentures and accrued interest thereon.
>
> 4. Sedren, S. A. to purchase from Continental 60,000 of its 5% Preferred shares at the par value thereof, namely $25.00 U.S. per share, subject to the listing thereof on the New York Stock Exchange, and in payment therefor Sedren, S. A. to issue to Continental a prior first mortgage on its assets in Haiti in the aggregate principal amount of $1,500,000 U.S. bearing interest at 6% per annum, payable half-yearly and maturing in five years with a provision for sinking fund payments of $300,000 per year subject to increase out of profits of production.
>
> 5. Sedren, S. A. to borrow from The Marine Midland Trust Company of New York and/or other banking institutions $1,100,000 U.S. repayable out of the profits of production together with interest at 6% per annum maturing in full in two years against the secu-

* Gordon, a New York lawyer for many years, was the senior partner of the New York law firm of Gordon, Brady, Caffrey & Keller, Continental's general counsel.

rity of the said 60,000 Preferred shares of Continental, and the said prior first mortgage of $1,500,000 would be subordinated to the $1,100,000 bank loan or assigned as collateral if required."

In addition, Gordon informed the Board that (166A):

"Mr. Gordon stated that an increase in the number of directors was desirable *so that Continental might have five nominees elected thereto*, the debenture-holders two (one from National Outlook Corporation and one from Mogul), and four representing the shareholders at large. This meant that eleven seats were necessary and the by-laws of the Company would require amendment accordingly. It was felt that a quorum should be five and that provision should be made for an Executive Committee of not less than three directors."

Gordon's recommendations were adopted in full on June 20, 1961, at which time a new by-law was adopted to provide for a Board of 11 directors, of whom five would form a quorum. *On that day, Gordon, Harris, Knorr, Ungerleider and Wheeler, the five Continental nominees selected by Continental's Board (Gordon, pp. 139-141) were elected to Halliwell's Board.* In addition, Gordon insisted that Mogul surrender its contract with Halliwell, "as managers, consultants and selling agents so that Continental could thenceforth take an active part in the management of the Company and Sedren . . ." (Pltffs Ex. 16 for Id., 165A; Gordon, 138-139)

Shortly thereafter, and on August 10, 1961 (Pltffs Ex. 13 for Id., 156A-158A), Continental's mining engineer and expert, George Tower (Gordon, 92; Knorr, 60) was "appointed to direct Sedren's mining and production organization . . ." (Gordon, 117; 158-159; Graetz, 299-301; Pltffs Ex. 13 for Id., 157A). On the same day, Halliwell's prior banking resolutions were rescinded and the signatories upon Halliwell's bank accounts at the Marine

Midland Trust Company of New York and the Royal Bank of Canada were revised to permit *only Continental officers and personnel as such signatories.* (Knorr, 77-78; Graetz, 320-322; Pltffs Ex. 13 for Id., 157A-158A; Pltffs Exs. 18 & 19 for Id., 170A-172A)

Upon the consummation of the June 1961 financing, Continental was in complete control of Halliwell-Sedren. The levers of that total control may be summarized as follows:

(1) Continental was the largest single stockholder of Halliwell, owning more than 1 million shares of that Company's common stock;

(2) Continental held a first mortgage of $1,500,000 upon the Sedren mine;

(3) Five of Continental's nominees now sat upon the Halliwell Board of 11; a sixth, Murray Cooper, was the brother-in-law of Harris, a Continental director; and the seventh, Graetz, was a fellow director of Gordon and Harris on the National Outlook Board;

(4) Tower, Continental's mining consultant and expert, and Kennedy, Continental's Vice-President, were now in complete charge of the operation and direction of the Sedren mine;

(5) Only Continental officers and personnel were signatories upon Halliwell's bank accounts and only they could disburse any monies for its operations. Knorr, Continental's Treasurer and Vice-President, boasted that, in his control of Halliwell's finances, he ran a very tight ship (Knorr, pp. 112-113). Continental controlled the financial affairs of Sedren (Knorr, 77-78; 99) and dealt with Sedren as though it were a division of Continental (Knorr, 138). The funds of Sedren on deposit in the United States were under Con-

tinental's control (Knorr, 122). The Halliwell-Sedren checkbooks and bankbooks were in Continental's physical possession and custody (Castro, 35-36; 54). No Halliwell-Sedren money could be expended for any Halliwell-Sedren purpose without the prior consent of Continental (Knorr, pp. 110-111).

(6) Finally, Halliwell was already in default under the April 1959 contract since it had never complied with the requirement that, commencing with the month of January, 1961, it deliver not less than 1,500,000 pounds of wire bar per calendar month. (Gordon, p. 160) It was therefore vulnerable at any time to Gordon's claim that it had breached the April 1959 agreement and was liable in damages to Continental for that default.

Gordon did not hesitate to inform Continental's stockholders publicly that Continental had acquired and was managing the Sedren mine. On October 26, 1961, at the annual meeting of the Continental stockholders, Gordon told them (Pltffs Ex. 20 for Id., 173A-174A):

> ". . . that *the purpose of the acquisition of Sedren was to obtain a controlled source of copper without the expenditure of great sums for exploration and development.* He further stated . . . that it is the opinion of the Company's engineers that the property was not properly managed prior to *the takeover by the Company.* However, in the short time that *the Company has been managing the mine*, it has been made into a profitable operation."

Further, in the annual report of Halliwell for the year ending December 31, 1961, addressed to the stockholders of Halliwell, of which Continental was then the largest, by a Board of Directors which contained five of the Continental nominees, it was stated (Pltffs Ex. 8, 125A):

"Modifications and introduction of new technical procedures by Continental Copper & Steel Industries, Inc. *following that organization taking over management control in August 1961* gradually whittled away at problems and they became resolved."

(4) Continental's Management of the Sedren Mine from June of 1961 until the Execution of the 1964 Continental-Halliwell Sedren Contracts

It became increasingly clear to Continental long before June of 1964 that, with the steady shrinkage of proven ore reserves, the Sedren mine could not possibly produce the 80 million pounds of copper which it was required to deliver under the 1959 contract. (Knorr, pp. 277-278). Moreover, the failure of the mine production to generate sufficient cash to permit the expenditure of adequate monies for the proper maintenance and/or replacement of worn out mining equipment and machinery, made it obvious that, even if 80 million pounds of copper ore were available at the mine, it could not conceivably be delivered to Continental by the contract date.

The reports of Continental's Tower, in complete charge of the management of the mine since August of 1961, were dismal. For approximately a year prior to April 30, 1964, Tower characterized the Sedren operation as a "thin-ice" operation.* Subsequently, in a personal report to Gordon dated April 30, 1964, Tower informed Gordon (Pltffs Ex. 21 for Id., 175A-178A):

"In conclusion, the writer feels a change of nomenclature for the Sedren's operation is in order. For the past year it has been called a 'thin-ice operation; i.e., earnings and production would be maintained only if some upset in operations were avoided which would

* None of Tower's personal reports to Gordon were submitted to the Halliwell Board. Copies were sent to Kennedy alone. (Gordon, pp. 195-196).

> 'break the ice'. I believe now a more applicable term is '*tissue thin*' operation." (178A)

In that same report, Tower informed Gordon (176A): "Summarizing, the end of the mine can be seen approaching rapidly. The bulk of the ore bodies have been depleted . . . and existing mining might be termed *scavenging the remnants.*"

Because of the Company's financial stringencies, Halliwell was continuously compelled to seek financial relief from and after 1962. It applied to the Haitian government for, and obtained, a moratorium upon the payment of the required royalties under the mine concession. It sought and procured a deferment of interest payments from the debenture holders. Finally, Harris and Graetz, two Halliwell directors, turned to Continental for some measure of relief from the provisions of the 1959 contract and Continental's control of Halliwell's finances and resources.

Gordon conceded that, during the discussions which preceded the execution of the 1964 agreements, Harris and Graetz had requested concessions and modifications from time to time from Continental "*to improve the situation for Halliwell*" (Gordon, pp. 240; 329; 226). The requested concessions included the reduction or elimination of the discount being paid to Continental by Halliwell, as well as the elimination of the liquidated damage clause. Gordon's response to those requests, then and thereafter, was stated by him as follows (Gordon, pp. 226-227):

> "Q. What was your response to those requests? A. That we had a valid and binding contract and I expected it to be lived up to."

When it was sought upon his deposition to ascertain the basis for his statements to Harris and Graetz that "we (Continental) had a valid and binding contract", the following transpired (Gordon, pp. 227-228):

"Q. Had you received any legal opinion from any counsel for Continental that it was a valid and binding contract? A. I have no specific recollection of it but generally, yes.

Q. And who was that counsel? A. Let's see—this is 1963?

Mr. Akers: 1964.

A. (Continuing) I believe it was the old firm of Gordon, Brady, Caffrey & Keller.*

Q. Can you recall who it was in that firm who expressed this legal opinion to you? A. No. I can't recall. I think it was the general opinion of the firm.

Q. Was it an opinion set down in writing? A. I have no recollection of it but I believe at some time or other there was a written opinion.

Q. Was that written opinion transmitted to the Board of Directors of Halliwell? A. I do not know."

By July 1, 1964, Sedren had only been able to deliver 38,556,000 pounds of wire bar under the 1959 contract, i.e., *somewhat less than one-half of the 80 million pounds specified in that contract* (Gordon, p. 233). Prior to the terminal date of that contract, Gordon had been alerted by the Tower report of April 30, 1964 to the fact that the "end of the mine can be seen approaching rapidly" and that "existing mining might be termed *scavenging the remnants*". (176A)

A decent regard for the fiduciary obligations which Gordon and the other Continental nominees owed as directors of Halliwell should have at least prompted an inquiry, prior to the execution of the 1964 Halliwell-Sedren-Continental contracts, whether it would be physically possible for Halliwell-Sedren to produce the balance of the 80 million pounds of copper after June of 1964 which they had been unable to produce prior thereto. No such inquiry was made (Gordon, p. 235), in spite of the fact that, as

* The firm was Gordon's law firm, Continental's general counsel.

Knorr admitted, "After a certain period of time had elapsed under the contract, under the original contract, and it appeared that the 80 million pounds would not be met under the terms of the contract (the 1959 agreement) . . . it did not appear, I think, to many people, in Continental, at least, *that Sedren ever would be able to fulfill that contract as far as the 80 million pounds are concerned . . .*" (Knorr, pp. 277-278). According to Knorr, "*There was always a question to me whether Sedren could meet that 80 million pounds, I think in most everybody's mind*" (Knorr, p. 277).

If, in fact, as Knorr testified, it was evident that the basic premise upon which the 1959 contract had been predicated, to wit, the existence of an estimated 80 million pounds of copper in the Sedren mine, was erroneous and that Halliwell-Sedren could not possibly produce and deliver what did not exist; if, in fact, the shared assumptions of both parties to the 1959 contract proved unfounded, the impossibility of that performance would necessarily relieve Halliwell-Sedren of their obligations under the 1959 contract.

Neither Gordon nor any other of the Continental nominees who served as Halliwell directors paid any attention whatsoever to their obligation to protect and defend the interests of Halliwell and its stockholders. Their total indifference to that obligation was conceded by the District Court in its opinion that the Continental nominees upon the Halliwell Board were acting as such "as agents or servants of Continental by whom they were employed" and "Indeed, the record and the depositions indicate that they were serving the interests of Continental . . ." (49a).

The Continental nominees completely disregarded the fact that, whatever may have been the situation in 1959, any negotiations between Continental and Halliwell in 1964 could not possibly be at arm's length. Gordon was adamant in insisting, as he swore at pp. 7-8 of his affi-

davit submitted in support of Continental's motion for summary judgment before Judge Owen:

> "Since by June 30, 1964, only 38,556,000 pounds of copper had been delivered, CCS could have terminated the wirebar agreement and demanded approximately $800,000 in liquidated damages."

Gordon's insistence, continually voiced, that the 1959 contract was a valid and enforceable agreement which gave Continental an absolute right in 1964 to demand from Halliwell liquidated damages in the sum of $800,000 was sufficient to still any effective opposition from anyone on the Halliwell Board to Continental's demand that Halliwell accept the terms and provisions of the 1964 agreements.

II.

The Corporate Opportunity of Which Halliwell Was Deprived by Continental Under the 1964 Agreements.

We now turn to a review of both the genesis and specific provisions of the Halliwell-Sedren Continental contracts of July 1, 1964 ("the 1964 agreements"). June 30, 1964 was not only the terminal date of the April, 1959 contract; it was likewise the terminal date of the Phibro contract of December 31, 1959.*

Approximately four or five months prior to the expiration of the 1959 contract, Thomas J. Kennedy ("Kennedy"), Continental's Vice-President, was instructed "to scout the market generally for the best possible smelting and refining terms." (Kennedy, 138-139; 156-157) After inquiring of Mitsui, the Japanese trading company, he was contacted by a representative of the Nippon Mining Com-

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* The Phibro contract was the Halliwell-Sedren contract with Phillipp Bros. Ore Corp. (Phibro), under which Phibro converted the Sedren concentrates into wire bar for delivery to Continental.

pany ("Nippon"). (Kennedy, 138) No representative of Halliwell-Sedren was asked to be present at any of Kennedy's discussions with the Nippon representatives (Kennedy, p. 152) and he could not assign any reason why he did not do so. (Kennedy, p. 152) Nor did he furnish Halliwell-Sedren with any of the written communications to and from Nippon. (Kennedy, pp. 92-94).

Although Kennedy had been directed to scout the market for Halliwell (Kennedy, 156-157) the written proposal which Kennedy obtained from Nippon was a proposal *not* addressed to Halliwell but to Continental. The contracts which were thereafter consummated with Nippon were *not* executed by Halliwell but by Continental. Those contracts with Nippon were *not* limited to "smelting and refining terms" (Kennedy, p. 138); they encompassed the complete disposition of all Halliwell-Sedren concentrate production from July 1, 1964 to December 31, 1966.

On May 14, 1964, Continental submitted to Halliwell, in writing, "our firm bid for two and one-half years production of the Sedren mine, commencing July 1, 1964". The firm bid was signed by Knorr on behalf of Continental. Kennedy participated in the preparation of that bid; it was reviewed, prior to its transmittal, by Gordon, Kennedy and Keller. (Kennedy, pp. 159-160)

The bid was considered by Halliwell's Board of Directors at its meeting on May 26, 1964. (Pltffs Ex. 12 for Id., 152A-155A) Gordon informed the Board that Continental had offered Halliwell a contract on May 14, 1964 *"based on a back to back offer from Japanese interests to purchase Sedren's production for a period of two and one-half years"*. (153A) The offer to which Gordon referred from unspecified "Japanese interests" was *not* exhibited by Gordon to Halliwell's Board nor were the Japanese interests named by him. Plainly, by his use of the words *"back to back offer"*, Gordon was advising the Halliwell Board *that Continental was passing on to Halliwell, as a*

conduit, the exact terms and provisions of the offer which Continental had received from the unnamed Japanese interests for the Sedren concentrate production for the two and one-half year period from June 1, 1964 to December 31, 1966.

However, the two contracts executed by Continental and Nippon, one encaptioned "Conversion Agreement" (Pltffs Ex. 24, 191A-201A) and the other encaptioned "Concentrates Agreement" (Pltffs Ex. 23, 181A-190A) granted Continental an enormously beneficial right which Continental did *not* pass on to Halliwell-Sedren. Continental obtained the right under its contracts with Nippon to divert and sell one-third of the concentrate production to any non-Japanese market anywhere in the world if the price prevailing thereat was a price higher than that which Nippon had agreed to pay ("the diversion right" or "the right of diversion"). (Pltffs Ex. 23, 181A)

The two Continental-Halliwell-Sedren agreements of July 1, 1964 (Defts Ex. E, 269A-273A; Defts Ex. F, 274A-283A) contained no such right of diversion. (Kennedy, p. 167) Kennedy conceded that, *to the extent of the diversion clause*, the Continental-Nippon contracts and the Continental-Halliwell-Sedren contracts were *not* back to back agreements. (Kennedy, pp. 167-168) Kennedy likewise conceded that there was nothing in the Continental-Halliwell-Sedren agreements which alerted Halliwell to the fact that Continental had a right, under its agreements with Nippon, to divert one-third of the Sedren production and sell that one-third at higher prices in non-Japanese markets. (Kennedy, p. 170)

Kennedy agreed that the right to divert one-third of the Sedren production was "a trading benefit" (Kennedy, p. 175) and that "There were damn few people who were receiving a one-third option from Japanese smelters to divert, to sell into other markets". (Kennedy, p. 175) He likewise conceded that "a good deal of income was derived by Con-

tinental from this diversion clause". (Kennedy, p. 176) There was no suggestion at any time that the trading benefit which Continental had envisioned from the income derived by Continental from the diversion clause should be shared in any way with Halliwell. (Kennedy, 176)

Although Kennedy admitted that, at the time he had been authorized to "scout" the market, he was representing Halliwell, as well as Continental, he did not ask for the diversion clause on behalf of both Halliwell and Continental (Kennedy, pp. 177-178). The diversion clause was requested and obtained by him solely for the benefit of Continental (Kennedy, pp. 177-178). His rationale for Continental's total appropriation to itself of the right to divert was the claim that Halliwell was still bound to deliver the balance of the 80 million pounds of wire bar under the 1959 contract (Kennedy, pp. 182-183). As noted above, no thought whatsoever was given by the Continental nominees to the fact (i) that Halliwell-Sedren may have been relieved of that obligation by the mistaken assumptions and estimates upon which that contract was based or (ii) that Halliwell was entitled to share in the inordinate profits of that diversion.

As Kennedy admitted, the diversion clause which Continental appropriated for itself in its 1964 contracts with Nippon, as well as in its 1967 contracts with Nippon, to the complete exclusion of Halliwell-Sedren, was enormously profitable to Continental (Kennedy, p. 176). *During the first year following the execution of its 1964 contracts with Halliwell-Sedren*, as reported by Continental to its stockholders in its annual report for the year ending June 30, 1965 (Pltffs Ex. 22 for Id., 179A-180A), *Continental earned a profit of $557,791.00 under the diversion clause.* (180A) Subsequent years were equally profitable. *The total amoun of the diversion profit realized by Continental from July 1, 1964 to March of 1968 under the diversion clauses in the 1964 and 1967 contracts was the total aggregate*

*sum of $1,394,977** (Pltffs Ex. 25, 202A-203A). Needless to say, neither Gordon nor Kennedy ever informed Halliwell of how much Continental had earned under that diversion clause (Kennedy, p. 195; Gordon, p. 248).

On the contrary, Continental deliberately withheld any information from Halliwell concerning the profits which it was realizing under its contracts with Halliwell. Thus, Carlos Castro, the Continental senior auditor charged with the responsibility of auditing the Continental-Halliwell-Sedren 1964 and 1967 contracts and computing in the document which he prepared on May 12, 1970, after this action was commenced, encaptioned "CCS Profits Effected on Purchase of Concentrates from Sedren, S.A." (Castro, 129-132; Pltffs Ex. 25, 202A-203A) the amount of profit realized by Continental testified as follows (Castro, 101-104):

> "Q. Now, . . . the fact of the matter is, is it not, that these (profit) figures which appear upon the first sheet of all the settlement documents in shipment 28 through 58 were not disclosed by you to anybody connected with Sedren and Halliwell? A. That's right.
>
> Q. Were you ever asked by anybody connected with Sedren and Halliwell for any such figures? A. Yes, I think I may have been.
>
> Q. By whom? A. Probably Mr. Graetz.
>
> Q. And what did you tell Mr. Graetz when he asked you for those figures? A. *Well, I probably smiled sweetly and said nothing.*
>
> Q. Well, I am sure, Mr. Castro, that you smiled sweetly, of that I am absolutely certain, but when you said nothing, didn't he press you for an answer? A. *I can be very evasive when I want to.*

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* Continental's total profit of $1,394,977 under the diversion clause in the 1964 contracts, which was continued in the 1967 contracts, was far in excess of the liquidated damages of approximately $800,000 claimed by Gordon in June of 1964.

Q. *And in that instance, when you were asked for those figures by Mr. Graetz, you were evasive?* A. *Yes. I am sure I was.*

Q. And did not make the disclosure to him that he requested? A. No.

Q. Is that correct? A. Absolutely.

Q. *You absolutely did not?* A. *I did not.*

Q. Can you tell us how many times or how many occasions Mr. Graetz made that request of you? A. I don't think very often.

Q. What would you say was not very often? Was it three, four, ten, twenty? A. In the course of 1964 through '68, perhaps three or four times, to my recollection."

In its opinion, the Trial Court summarized the losses sustained by Halliwell in 1964 to 1968, the period encompassed by the 1964, 1967 and 1968 agreements (45a). Those losses, predicated upon Halliwell's audited financial statements for those years, were as follows:

1964	Loss	$1,164,280
1965	"	$1,142,891
1966	"	$1,169,076
1967	"	$1,674,931

The overall aggregate of those losses during those years was the sum of $5,151,178. Those calamitous losses occurring under Continental's absolute control of Halliwell-Sedren must be compared with the profits realized by Continental from the Sedren concentrates during that very same period which were computed on May 12, 1970 by Castro, after the institution of this action, for the purpose of advising Continental's principal officers of the financial benefits realized by Continental under its Halliwell contracts. Those computations (Pltffs Ex. 25, 202A-203A) were verified by Castro, under oath, as true and correct in all respects (Castro, 84, 87-88, 211-212).

They show that Continental realized a profit from the Sedren concentrates of $1,394,977.40 and an aggregate discount in the sum of $859,879.97, making a total of $2,254,857.37. In addition thereto, Continental procured from Halliwell under the March 1968 agreement liquidated damages in the sum of $323,868 and additional discounts of $109,836, making an aggregate addition to their previously realized profit of $433,704. Adding both figures, the record conclusively established that, during the period that Halliwell had suffered a disastrous loss of $5,151,178, Continental had realized an overall profit in the sum of $2,688,561.37, figures which speak far more eloquently than any words can possibly express, the extent of Continental's depredations and the magnitude of Halliwell's losses during the period that Continental managed, controlled and administered the finances and affairs of Halliwell.

We now turn to a consideration of the manner in which Continental allegedly procured what purported to be the Halliwell Board's approval of the Halliwell-Sedren-Continental contracts of July 1, 1964. The Continental offer of May 14, 1964 was presented to Halliwell's Board for acceptance on October 8, 1964. (Pltffs Ex. 30, 233A-234A; Pltffs Ex. 11 for Id., 149A-151A) At that meeting, *nine Halliwell directors were present, five of whom were Continental nominees*: Gordon, Harris, Ungerleider, Wheeler and Knorr. The remaining four were Graetz, Bell, Cooper and Fell. Under Article VIII of the Halliwell By-laws, it was provided (Defts Ex. P, 370A-379A):

> "ARTICLE VIII—DISCLOSURE OF INTEREST BY AND PROTECTION OF DIRECTORS AND OFFICERS
>
> In supplement to, and not by way of limitation upon any right conferred upon directors by Division XXV of the Quebec Companies Act, it is declared that . . . *nor shall any contract or arrangement entered into by or on behalf of the Company in which any director or officer shall be in any way interested be voided,* nor

shall any director or officer be liable to account to the Company for any profit arising from any such office or place of profit or *realized by any such contract or arrangement by reason of the fiduciary relationship* existing, *if such director or officer has made a declaration of his interest and has not voted in respect of any such contract or arrangement.* For the purposes of this Article VIII, a general notice given to the director of a company by a director or officer to the effect *that he is a shareholder of or otherwise interested in any other company,* or is a member of a specified firm and is to be regarded as interested in any contract or arrangement made with such company or firm shall be deemed to be a sufficient declaration of interest in relation to any contract or arrangement as made."

As noted above, under Article III (a) of Halliwell's By-laws, of the eleven-man board of Directors, "five shall constitute a quorum". (371A) Consequently, on October 8, 1964, when the Board met to consider the Halliwell contracts with Continental as of July 1, 1964, *the quorum of five required by Article III (a) of the By-laws did not exist* since *all five Continental nominees were disqualified from voting.* Only four of the Halliwell directors present on that day, Graetz, Bell, Cooper and Fell could be considered in determining the existence of a lawful quorum or lawfully empowered to vote upon the matters then before the Board. Since, under Article IV, subdivision (d) of the Company's By-laws, if a proper quorum existed, "all questions arising at any meeting of the directors shall be decided *by a majority of votes*", the four remaining directors did not constitute *either a quorum or a majority* of those present at the meeting which was necessary to validate any corporate action by the Board on that day.

However, in order to procure the necessary five for quorum and vote, *Knorr did in fact vote,* although Gordon, Harris, Ungerleider and Wheeler announced that, with re-

gard to both agreements with Continental, they could not vote thereon. Knorr voted to approve the execution of those contracts with Continental (Knorr, p. 195), *in spite of the fact that he was the Treasurer and Vice-President of Continental and one of the five Continental nominees upon the Halliwell Board.* Indeed, the contracts of July 1, 1964 were executed on behalf of Continental by Knorr himself. (Knorr, 211-213) *Without Knorr's improper inclusion in the assumed existence of a lawful quorum and his vote in support of Halliwell's approval, the July, 1964 contracts were not merely voidable; they were absolutely void.*

Knorr's participation in the vote on that occasion was sought to be justified by both Knorr and Gordon upon the ground that he was not disqualified from voting at that time because he was only an officer of Continental, and not a director (Gordon, pp. 241-244), notwithstanding the fact that the By-Laws of Halliwell prohibit any vote by "a director or officer" if "he is a shareholder or otherwise interested in any other company", in which event he "is to be regarded as interested in any contract or arrangement made with such company. . ." If such an "interested director or officer" voted upon the resolution, particularly where his vote was indispensable to its approval, the contract was absolutely void.

Gordon's disdain for the principle that Knorr, Continental's Treasurer and Vice-President, was disqualified from voting as a Halliwell director to approve, on behalf of Halliwell, the contracts with Continental of July 1, 1964 is apparent from his testimony that "it is not a fact that he [Knorr] should not have voted on it either: that is politician's stuff". (Gordon, 241-243)

Knorr's vote as a Halliwell director to approve a contract which he had executed on behalf of Continental pursuant to the mandate of the Continental Board was completely illegal. It would be difficult to conceive of a more thoroughly tainted and invalid contract than that procured

by Knorr's vote on October 8, 1964, in complete disregard of the Halliwell By-Laws which explicitly provided what the law itself commands.

III.

The Defendants' Violation of Their Fiduciary Obligations to Halliwell-Sedren by Their Exaction of the 1967 Agreements and General Releases.

Prior to the expiration of the 1964 agreements, discussions took place between Continental and Halliwell with respect to the terms of the contracts which would cover the period from and after January 1, 1967 (Gordon, 254-255). In those discussions which commenced several months before January 1, 1967, Gordon, Kennedy and possibly Keller were speaking for Continental (Gordon, 255). Harris and Graetz asked that the price of future Sedren concentrates be fixed at the London Metal Exchange (LME) price because it was "higher, obviously" (Gordon, 257). They were pressing for that price, said Kennedy, for its additional revenue "for Halliwell" (Kennedy, 211).

At a meeting of the Halliwell Board of Directors on December 14, 1966, Knorr presented a cash flow statement of Sedren for the period from December 1, 1966 to June 30, 1967, annexed as Schedule B to the minutes of that day (Defts Ex. V, 495A-503A; Bell, Tr. 39-50). We quote from the minutes as follows (496A):

> "SEDREN, S. A.
>
> *Finance Position*
>
> Mr. Walter H. Knorr then presented to the meeting a cash flow of Sedren, S. A. for the period from December 1, 1966 to June 30, 1967, a copy of which is appended as Schedule 'B' to these minutes. Mr. Gordon asked what price was used for the production

of copper subsequent to December 31, 1966. Mr. Knorr replied that a price of 48¢ per pound of copper was used. *Mr. Gordon then stated that the cash flow has no meaning because Sedren would not receive this price for copper after December 31, 1966.* He stated that Continental Copper & Steel Industries, Inc., was going to insist on the delivery of wire bars effective January 1, 1967, in accordance with the contract dated April 1, 1959, as amended.

The price of 48¢ per pound of copper upon which that cash flow report was based was the Engineering & Mining Journal (E & MJ) export price at that time, a price favored by Kennedy (Kennedy, 242). That price was lower than the LME price (Kennedy, 217) for which Harris and Graetz had asked (Kennedy, 214-215).

On December 28, 1966, while these discussions were in progress, *Gordon caused to be served upon Halliwell a formal written demand by Continental that Halliwell commence delivery of wire bar effective January 1, 1967*, only three days later, in accordance with the April 1, 1959 contract (Pltffs Ex. 29, 230A-232A; Pltffs Ex. 30, ¶ 26, 234A). That written demand proposed an alternative, to wit, Continental's willingness to accept delivery of copper concentrates in lieu of wire bar *at a price of 32½¢ per pound.* It was obviously impossible, and known by Gordon to be impossible, either for Halliwell-Sedren to commence delivery of wire bar on January 1, 1967 or to survive at a price of 32½¢ per pound.

At that time, *the cost of producing a pound of copper by Sedren*, according to figures prepared by Carlos Castro, Continental's senior accountant and presented by Knorr, Continental's Vice-President and Treasurer, to the Halliwell Board at its meeting on December 14, 1966, *was in the area of 35 to 36 cents per pound* (Bell, Tr. 51-52). Consequently, *the price of 32½¢ per pound of copper* specified in Continental's written demand of December 28,

1966 *was less than Sedren's actual cost of production, minus charges* (Bell, Tr. 52). Gordon was fully familiar at all times with Sedren's cost of producing copper at the mine (Knorr, 60).

The service of Continental's demand of December 28, 1966 was deliberately calculated to terrorize the Halliwell directors into the acceptance of any contract dictated by Gordon and Continental for the period subsequent to December 31, 1966. Gordon's brutal indifference to whether Halliwell-Sedren could or could not comply with his demand that it commence the delivery of wire bar on January 1, 1967 or furnish copper concentrates as an alternative at a price of 32½¢ per pound was not only established by his own testimony (Gordon, 288-289), but by the sworn statements of Adolph Graetz as well.*

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* Graetz who was not permitted by the Trial Court to testify was, therefore, unable to testify at the trial to the following facts to which he had sworn at pp. 21-22 of his affidavit submitted to Judge Owen upon the motions for summary judgment:

> "It was obviously impossible, and Gordon knew that it was impossible, for Halliwell-Sedren to furnish any amount of wire bar on three days' notice. Gordon knew that, in order to comply with such a demand, negotiations would have had to be undertaken with some company many months before December 31, 1966 to produce the wire bar which he demanded; that such negotiations would take many weeks; and that, after the negotiation of such a contract, the delivery of the concentrates and its conversion into wire bar would take many more weeks, as well as the time consumed for delivery to Continental. His purpose, and it completely succeeded, was to terrorize the directors of Halliwell into an acceptance of his demands because they possessed no other possible alternative. In a letter to Cooper dated January 9, 1967, Fraser Fell, a director, expressed the feeling of all of the non-Continental directors that Gordon's insistence upon the delivery of wire bar at the price which he specified "would undoubtedly result in the insolvency of Sedren" and that, in the absence of any other viable alternative, 'it is imperative that a compromise agreement be reached with Continental' (Ex. 45)."

Before turning to a consideration of the only agreement that Gordon would tolerate, and the manner in which that "agreement" was forced down the Halliwell throat, it is necessary that we note Gordon's violent fury that Harris and Graetz had dared to oppose him in their efforts to improve Halliwell's position. Gordon testified as follows (292; 296-299):

> "Q. Did you tell Mr. Harry Harris that it was a negotiating position, and to regard it (Continental's demand of December 28, 1966) merely as that? A. Certainly not. Mr. Harris was an antagonist and he was trying to get the LME price, and I was just as firm, we were not going to accept the LME price, and we insisted on the 1959 contract, and the negotiation which resulted was a compromise between the two.
>
> Q. Now, you said before, at a prior session of this examination, that Mr. Harris was antagonistic and you repeated those words here. Did you regard Mr. Harris as being an antagonist in the month of December, 1966, in connection with these matters? A. I regarded Mr. Harris as wearing three or four hats. *His principal interest was* to get the best deal he could for *Sedren and not the best deal for Continental.*
>
> • • •
>
> Now, Harris knew what my position was in the beginning, *and these letters were part of the negotiating pressure that we were applying.*
>
> They were applying their pressures, and *we were applying ours.*
>
> Q. Now, what pressures were they applying? A. Negotiating tactics and stratagem.
>
> Q. What pressures were you applying? A. Taking a position. This is the position we were taking. We wanted the contract of 1959 to be honored. That was our position. That is where our strength came from. *They were giving us reasons why this was a disadvantageous contract for the company at this point in*

time, and we said, we will not argue with you, whether it is an advantage or disadvantage.

That was a different subject all together. Here is a contract, we are consenting to make these adjustments. We took this position, and they took the other position.

They exercised every type of accusation that they could exert. And I took the position that this was a contract which was valid, and should be honored . . .

Q. Now, you said something during the course of your answer which I am not quite sure I understood, you said something about the fact that they used every kind of accusation.

What was the accusation? A. The usual.

Q. Just tell me, I don't know what the usual accusations are? A. I have no precise recollection, but Graetz, who was one of the ring-leaders claimed either mismanagement or—the usual diatribe. When you have made a contract—

Q. Mr. Gordon, I don't know what the words 'usual diatribe' mean. A. I will have to withdraw them; I don't either. I am just saying Mr. Graetz on occasion made sundry and various accusations.

Q. What were those accusations? A. I do not recall them.

Q. Did Mr. Harris make any sundry accusations? A. I don't think so.

Q. Did Mr. Cooper make any accusations? A. I think so.

Q. What kind of accusations? A. I don't remember.

Q. Okay.

Did Mr. Bell make any accusations? A. Not that I recall.

Q. Did Mr. Fell make any accusations? A. Not that I ever heard.

Q. Did any other member of the Halliwell Board make any accusations? A. Not that I recall."

As appears from his testimony, Gordon's stance at that time was hardly that of a man who was endeavoring in good faith to discharge his fiduciary obligations as a director of Halliwell. It was, on the contrary, the posture of a man battering an enemy into total submission by every weapon at his command.

Several months later, at a Halliwell Board meeting held on April 12, 1967, Gordon submitted a document dated April 5, 1967 encaptioned "Modifications to CCS, Halliwell-Sedren Contractual Obligations." (Pltffs Ex. 1, 60A-72A; Pltffs Ex. 30, 235A; Bell, Tr. 28-29) An examination of that memorandum disclosed the fact, as appears from the minutes, that the price formula provided in that memorandum would mean "that Sedren would receive approximately 41.8¢ per pound of copper . . ." . (60A) The memorandum also provided, in paragraph 8 thereof, that *"The parties will exchange general releases* excepting only the obligations under the concentrates agreement and copper purchase agreement as modified in accordance with the foregoing and excepting inter-company indebtedness." (69A)

Gordon's proposal was submitted on a, "this is it, take it or leave it" basis. (Cooper, 121; Graetz, 609) Halliwell was told that "this was a deal you are going to get and if you don't accept the deal you know the consequences as far as Halliwell and Sedren was concerned". (Cooper, 120) The consequences were insolvency. (Cooper, 121) Halliwell was faced with two alternatives, either to accept the Gordon proposal and try to make the best of it or reject it and suffer the consequences of insolvency for the company and its shareholders. (Cooper, 122) Cooper testified that "We were in the position where a gun was right at our head. . ." (Cooper, 120) "We were handed it (the Gordon proposal) at the point of a gun". (Graetz, 614-615)

The Halliwell directors were fully aware of the fact that the cost of operations at the mine in April of 1967 was about 41 or 42 cents a pound of copper (Graetz, 612). It

was impossible, therefore, for Halliwell-Sedren to survive under Gordon's dictated price of approximately 41.8 cents per pound of copper (Graetz, 612-613). Both Cooper and Graetz were persuaded by Harris, a Continental nominee on the Halliwell Board, to go along for the time being and not resign because he was hopeful of persuading Gordon to increase the price for the benefit of Halliwell-Sedren (Cooper, 123-125; Graetz, 610-611). Unfortunately, Harris died shortly thereafter (Cooper, 123-124).

The memorandum submitted by Gordon at that meeting was more than the other non-Continental directors could stomach. Bell, a non-Continental member of the Halliwell Board, declared at the meeting that the deal set forth in the memorandum dated April 5, 1967 was detrimental to Halliwell and Sedren because they were at that time virtually insolvent. He urged the Halliwell directors to challenge the validity of the 1959 contract (Bell, Tr. 34). Gordon responded that if the Board acted to repudiate the 1959 agreement, or contest the validity of the 1964 concentrates and wirebar agreements, the Company would have the juiciest lawsuit in the United States (Bell, Tr. 35).

Thereupon, after a recess, Gordon demanded and received the resignations of three non-Continental Board members, David W. Knight, Fraser Fell and Robert D. Bell, as well as Bell's resignation as Secretary of Halliwell (Pltffs Ex. 30; Bell, Tr. 35). As a result only eight directors remained* on Halliwell's Board of Directors at

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* Graetz swore at page 23 of his affidavit upon the motions for summary judgment, that:

> "Every attempt on the part of those who remained (after the resignations of Knight, Bell and Fell) to persuade Gordon to adopt a more reasonable course was completely unsuccessful. The minutes cannot possibly convey Gordon's domineering and bullying attitude. For example, at the time that it was proposed to vote upon the proposal, Wheeler, one of the Continental directors, stated that he would abstain from voting, at which point Gordon told him 'you can't do that' and that he must vote in favor of the proposal. Wheeler did so."

said meeting, the five Continental nominees and Messrs. Cooper, Graetz and Baussan, the director from Haiti (Pltffs Exs. 1; 30; Bell, Tr. 35-37).

Resolutions providing for the approval and authorization by Halliwell and Sedren of the new contracts and general releases, as provided for in the aforesaid memorandum dated April 5, 1967, were then drawn at the meeting by Herman Keller, Continental's Secretary and General Counsel (Pltffs Exs. 1, 60A-72A; and 30, 235A). Gordon asked Keller if the Continental nominees could vote as members of Halliwell's Board upon the resolutions and Keller's answer was yes. (Bell, Tr. 36)

Gordon, Wheeler, Ungerleider, Harris and Knorr then voted to approve the execution of the contracts and releases proposed by Gordon. Baussan abstained from voting. In voting for the resolutions upon the urging of Harris, Graetz declared "that while this was not the best contract for the Company, it was stopgap until a new one could be negotiated". It was never, of course, a stopgap.

Gordon, Harris, Knorr, Wheeler and Ungerleider, the five Continental nominees who, as Halliwell directors, voted to approve the 1967 contracts and releases, were absolutely barred as a matter of law under Article VIII of Halliwell's By-Laws from voting to approve any contract or arrangement between Continental and Halliwell. The only directors who were qualified to vote at that time were Messrs. Baussan, Graetz and Cooper. Mr. Baussan, the representative from Haiti, refrained from voting. Consequently, *only two valid votes* were cast in favor of the adoption of the resolutions instead of the five necessary to constitute a majority of those present. The contracts and releases purportedly authorized by *only two* of the Halliwell directors present on April 12, 1967 were in complete violation of the Article VIII heretofore set forth above. The contracts and releases purportedly so authorized, the latter constituting the basis for the defendants' defense herein, were a total nullity.

Upon his deposition, Gordon attempted to justify the unconscionable price upon which he insisted in the 1967 agreements by claiming that such a price would be sufficient "if the Sedren mine were operated correctly" (308), an extraordinary rationale since Continental's Tower had been in charge of the direction and operation of the mine on behalf of Halliwell since 1961. Gordon's response, predictably, was to blame Graetz and Cooper for Continental's mismanagement and incompetence (Gordon, 309-311).

Gordon's attempt to justify the price which he demanded for the 1967 contracts was demolished by Kennedy who conceded that Halliwell-Sedren could not exist with a price of 41.8¢ per pound for the copper production from the Sedren mine (Kennedy, 227-231). The price specified in the 1967 contracts covered the period commencing January 1, 1967. By April of 1967, Continental knew what the result of the price established by the contract formula would be as applied to the first three months of the 1967 Sedren operations. Kennedy admitted that the price established by the formula, as applied to the first three months of 1967, would not permit Halliwell to exist and that, if it continued beyond the first three months, Halliwell could not possibly survive. No suggestion was made at that time by anyone that a minimum be established for Halliwell so that it could at least survive with that minimum and not be reduced below a starvation level. Kennedy's testimony is explicit (Kennedy, 228; 229; 230-231):

> "Q. You just mentioned a moment ago that there were swings back and forth.
>
> Isn't it entirely possible that, if the swing persisted adversely for Halliwell, that it would be driven out of business because of the inadequacy of the price for copper? A. If the swing had persisted, yes, there is always that possibility.
>
> Q. What provision was made in any contractual arrangement with Halliwell from and after January

1967 to avert such a contingency? A. I don't believe there was anything, contractually."

We have heretofore noted that the resolutions of the Halliwell Board of Directors which were purportedly adopted at the Halliwell Board meeting of April 12, 1967 were allegedly approved by the vote of Gordon, Harris, Knorr, Wheeler and Ungerleider, Continental's nominees upon that Board. With the exception of Knorr's vote to approve the 1964 agreements, Halliwell's minutes are replete with innumerable prior instances where the same individuals, after disclosing their interest as officers, directors and shareholders of Continental, had refrained from voting at a Halliwell Board meeting which dealt with proposed contractual relationships between Continental and Halliwell (Gordon, 144-149).

Apparently, according to Gordon, the prior abstentions by the Continental nominees did not constitute any recognition on their part that such abstentions were required by law. They were, according to him, merely a matter of "*personal preference*" in which they could indulge or not as they pleased (Gordon, 148-149). They indulged in that "personal preference" whenever it appeared necessary to find an additional vote or votes by which to impose Continental's will upon Halliwell, as Knorr's vote did in June of 1964 and as the vote of Gordon, Knorr, Halliwell, Wheeler and Ungerleider did in April of 1967.

IV.

Continental's Exaction of the 1968 Agreements.

By June 22, 1967, Continental's mortgage on the Sedren property had matured with respect to both principal and interest (Pltffs Ex. 30, 236A). On July 18, 1967, the Board of eight directors was advised by the five Continental nominees that Continental was pressing for a settlement of its accounts (Pltffs Ex. 30, 236A).

By March of 1968, Halliwell was completely insolvent. Sedren's trade accounts were not being paid and were overdue. (Bell, Tr. 13-14) It was confronted with a defaulted mortgage held by Continental upon the Sedren mine of principal and interest aggregating the sum of $326,343.96. In addition, Continental demanded the payment of $323,868 in liquidated damages under the 1959, 1964 and 1967 agreements. It insisted, also, upon the payment of a discount in the sum of $109,836. Unless Halliwell, unable to meet any of these payments, appeased Continental in whatever manner Continental demanded, the Continental mortgage would have been foreclosed, the Sedren mine, Halliwell's only asset, would have been appropriated by Continental; and Halliwell would simply have ceased to exist.

Halliwell's overall economic position was catastrophic. It had sustained an operating loss of $1,674,931 for 1967, and its capital deficit at the end of December 31, 1967 was $5,422,196 (Pltffs Ex. 30, 236A). In addition, its outstanding debentures in the sum of $2,907,000 were in default as to principal and interest amounting, as of March 31, 1968, to the sum of $3,577,920.43 (Pltffs Ex. 9, 137A).

Throughout this period of time, while Halliwell was struggling desperately to stay alive, it was attempting in discussions with Gordon to free itself from its bondage to Continental by procuring a final termination of the 1959, 1964 and 1967 agreements with Continental. At page 25, paragraph 45, of his affidavit submitted to Judge Owen upon the motions for summary judgment, Adolph Graetz, whom the plaintiffs were not permitted by the District Court to call as a witness for the plaintiffs, swore to the following facts:

> "During this period of time, Gordon made it perfectly plain, on any number of occasions, that he intended to enforce Continental's alleged rights to the hilt unless Halliwell complied with his demands. In that event, if Continental dared to oppose his wishes, Halliwell

would have been extinguished. Consequently, the agreement of March 15, 1968, which was dictated by Gordon, was the price of Halliwell's survival. In its economic extremis, Halliwell had no choice whatsoever but to capitulate to Continental upon the terms dictated by Gordon."

The terms dictated by Gordon were calamitous. Continental insisted, as a condition precedent to any termination agreement with Halliwell, that the debenture holders execute an agreement, whereby they would cancel $1,308,150 of the principal amount of their debentures and accrued interest thereon and convert the remaining $598,850 principal amount of said debentures together with accrued interest thereon into shares of the common stock of Halliwell. He further insisted, as provided in the third Whereas clause of the proposed March 15, 1968 agreement between Continental and Halliwell, that "All of the aforesaid agreements (of 1964 and 1967) and *releases issued thereunder* are hereby ratified, confirmed and approved in all respects . . ." by Halliwell-Sedren.

Only upon the foregoing conditions would Continental agree, as more specifically provided in the termination agreement of March 15, 1968, to terminate the copper purchase and concentrates agreements, extend the dates for the payment of the principal and interest of the mortgage indebtedness, accept 359,100 shares of the common stock of Halliwell in payment of the liquidated damages claimed by Continental of $323,868; and accept from Halliwell the sum of $109,836 in installments in payment of the discount claimed by Continental. (Defts Ex. A, 243A-249A)

Prior to the execution of the agreement between Halliwell and the debenture holders, dated as of March 15, 1968, the financial condition of Halliwell was considered by the Board of Directors of Mogul, the holder of Halliwell debentures in the principal sum of $2,750,000. The Mogul Board concluded that, if Mogul did not accept the agree-

ment with Halliwell concerning its debentures, demanded by Continental as the condition precedent to Continental's proposed agreement with Halliwell as of March 15, 1968, there would be no agreement between Continental and Halliwell. (Bell, Tr. 17-18) They had no alternative but to go along with the arrangement because, to do so, would avert the immediate bankruptcy of Halliwell-Sedren at that time. (Bell, Tr. 17-18)

Gordon's threat that, unless Halliwell accepted the agreement tendered by Continental, Continental would foreclose its mortgage upon the Sedren mine was sufficient to compel Halliwell's surrender to Gordon's demand as the price of survival (Defts Ex. A, 243A-249A).

Thereafter, notice of an annual and special general meeting of shareholders, to be held on May 13, 1968, was sent to the stockholders of Halliwell, together with a consolidated balance sheet of Halliwell and accompanying financial statements for the year ending December 31, 1967, as well as a document encaptioned "Information Circular" (Defts Ex. M, 303A-317A). Attached to the Information Circular as Exhibits A and B were the agreements between the debenture holders and Halliwell, as well as the agreement between Continental and Halliwell. Under paragraph 6(b), the agreement between Continental and Halliwell was conditioned upon the approval by the shareholders of the agreement between Halliwell and the debenture holders.

The shareholders of Halliwell were further advised by Note 5 of the Consolidated Balance Sheet of the Company and accompanying financial statements for the year ending December 31, 1967, that (Pltffs Ex. 9, 137A):

"5. Current Liabilities:

> If the reorganization of the company (see note 4) is not approved, all of the non-current liabilities amounting to $3,960,018 at December 31, 1967 become due and payable immediately."

In the material sent to the shareholders, concededly not a word appears which could possibly alert the shareholders to Halliwell's right to recover from Continental for its depredations from June of 1964 to the date of the meeting. Indeed, the stockholders were asked to ratify the payment by Halliwell to Continental of liquidated damages in the sum of $323,868 for Halliwell's alleged failure to deliver 16,193,406 pounds of the 80 million pounds of copper required under the initial agreement without the slightest knowledge of the fact that the 1964 and 1967 agreements, and the April 1967 releases, executed under the circumstances then prevailing, were unconscionable and extortionate.

The March 1968 contracts between Halliwell and Continental and Halliwell and the debenture holders were approved by a vote of 3,637,875 shares out of 11,936,674 shares of the common stock of Halliwell then outstanding (Defts Ex. C, 259A), far less than a majority of Halliwell stockholders.

It was not until the Sedren mine had been freed from the possibility of foreclosure by Continental that Halliwell, for the very first time, was able to act upon the advice of outside independent counsel that it was entitled to recover from these defendants the full amount of the damages which it had sustained as a consequence of their inexcusable breaches of their fiduciary obligations to Halliwell and its stockholders (Defts Ex. AE, 525A-532A, at 531A).

In April of 1970, the present action was instituted by Halliwell against the defendants herein, the first time that it was possible to institute an action without incurring the unacceptable loss of the Sedren mine by Continental's foreclosure of its mortgage. In 1971, operations at the Sedren mine were completely suspended. In 1975, the Sedren concession was terminated by the Haitian government. The Sedren mine never yielded 80,000,000 pounds of copper despite eleven years of production.

As will hereinafter appear, the failure to fully inform the Halliwell stockholders at the annual meeting of Halliwell's rights against Continental, in the specific respects hereinabove reviewed, renders the releases voted by the Continental nominees to Continental under the 1967 agreements and the alleged settlement purportedly effected by the termination agreement of March 1968, a total nullity.

The Opinion of the Court Below

The opinion of the Court below (36a-55a) will be examined in vain for a single word which acknowledges *the fact that Continental and the five Continental nominees upon the Halliwell Board owed any fiduciary obligations to Halliwell and its stockholders.* On the contrary, it approvingly describes the acts of Continental and its nominees as acts permissibly performed by Continental in "Continental's desire to have Halliwell and Sedren live up to the 1959 contract. It may be that these efforts were heavy handed or that Continental, which had never operated a mine may not have fully understood the situation. However, there is no duress to the extent that Continental was seeking to stand on its prior legal rights". (51a)

The Court placed the burden of proving the invalidity of the 1967 releases and the 1968 agreement purporting to ratify those releases entirely upon the plaintiffs, citing Judge Mulligan's concurring opinion in *First National Bank of Cincinnati* v. *Pepper*, 454 Fed. 2d 626. (48a) It completely ignored the fact that, in *Pepper* as well as *Austin Instrument* v. *Loral*, 20 N.Y. 2d 124, there was no fiduciary relationship of any kind between the parties to the challenged documents. The District Court did not even advert to the principle, so firmly imbedded in prevailing corporate jurisprudence, that, in any transactions between one corporation and another with common directors, those dual directors bear the burden of satisfying

the Court that they had exercised an unbiased and unprejudiced judgment in good faith and that the transaction was not unfair and improvident to either Company (*Chelrob Inc.* v. *Barrett*, 293 N.Y. 442; reaffirmed in *Ripley* v. *International Railway of Central America*, 8 N.Y. 2d 430).

Although the Trial Court emphasized the fact that the plaintiffs called at the trial "as their only live witness Robert Bell of Toronto, Canada", the Secretary-Treasurer of Halliwell until April 12, 1967, and that "Mr. Bell testified as to his activity on the Halliwell Board of Directors and the reasons for his resignation from the Board on April 12, 1967" (38a); *the Court failed to mention the further fact that it had adamantly refused to allow the plaintiffs to call Adolph Graetz as a live witness* (Tr. 41-53), although Graetz, a Halliwell director continuously from 1961 to a date long past the date that this action was instituted, was prepared to testify in detail to the events which occurred before, during and after the execution of the Halliwell-Sedren-Continental contracts in issue, the execution of the April, 1967 releases and the March, 1968 termination agreement and the details of the agonizing economic extremis which confronted the Halliwell Board and compelled Halliwell to surrender to Continental's demands in 1967 and 1968. The Court's inexplicable and capricious refusal to hear the live testimony of Graetz, although it quoted from his deposition taken by the defendants,* was an error which alone warrants the reversal of the judgment appealed from.

The Court referred to the submission of the March, 1968 termination agreement to the stockholders of Halliwell. In noting that the Halliwell stockholders had not

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* The difference to the plaintiffs between the live testimony of a party or witness with an intimate and personal knowledge of all the facts and his deposition by an adversary limited solely to those narrow areas with which the adversary is restrictively concerned is too manifest to require extensive elaboration.

been fully apprised of the relevant facts and circumstances which had preceded the execution of the general releases and the termination agreement by its Board, the Court cast the duty of that disclosure upon the then Halliwell directors (54a), totally ignoring the fact that Continental and its five nominees were seeking thereby to escape the consequences of their breach of their fiduciary duties to Continental and Halliwell, and could only do so, if at all, by proving, at the very least, that the stockholders of Halliwell were fully informed of what they had been called upon to ratify.

There remains to be considered the District Court's statement in its opinion that Continental's threat to foreclose its mortgage on the Sedren mine "is not duress since it had every right to do so. Moreover, Continental did not foreclose but, instead, granted an extension of time in the 1968 Settlement Agreement" (56a, footnote 6). Had not Halliwell-Sedren been financially ravaged by Continental from 1961 to 1967, had it even been permitted a fair share of the $2,254,857.37 which Castro had computed as the "CCS Profits Effected on Purchase of Concentrates From Sedren S.A." (Pltffs Ex. 25, 202A-203A), there would not have been a defaulted mortgage or a bankrupt Halliwell. Continental's assumed legal right, as a trustee, to enforce the Sedren agreements did not confer upon it the right to manipulate Halliwell-Sedren for its own profit, and exact from an abused *cestiu* far more than was warranted by its pound of flesh. Continental did not foreclose only because, in March of 1968, it exacted everything that it desired from Halliwell-Sedren, including an alleged ratification of the April, 1967 releases.

Finally, although the District Court conceded that the five individual defendants, as Continental's nominees, were not parties to the 1967 releases or the 1968 termination agreement, they were nevertheless absolved of liability thereunder because, *firstly* "there has been no showing that they personally profited in any way by anything

that was done" (49a); *secondly*, and incredibly, that "they were acting as agents or servants of Continental by whom they were employed" (49a) and "that they were serving the interests of Continental in much the same way as the majority directors were seeking to serve the interests of Halliwell and Sedren" (49a-50a), *totally ignoring the fact that on April 12, 1967, when the 1967 contracts and releases were approved, the five Continental nominees constituted a majority of the eight man Halliwell Board;* and, *thirdly*, "if the 1967 releases to Continental were valid under New York law, their effect was to release the individual defendants." (50a)

The Court's conclusion that the five individual defendants, who, as Continental nominees served as Halliwell directors, were free to serve "the interests of Continental in much the same way as the majority of Halliwell directors were seeking to serve the interests of Halliwell-Sedren" constitutes an incomprehensible disregard of the most elementary principles of directorial responsibility for the duty of loyalty which they were required to observe in serving the interests of Halliwell and its stockholders. The full extent of the District Court's indifference to the fiduciary obligations of the Continental nominees upon the Halliwell-Sedren Board will be considered in greater detail in our discussion below of the authorities applicable thereto.

ARGUMENT

POINT I

The Defendants Are Liable for the Full Amount of the Damages Sustained by the Plaintiffs as a Result of Their Breach of the Fiduciary Duties and Obligations Which They Owed to the Plaintiffs.

In the instant case, Continental's absolute domination and control of Halliwell by and through the individual defendants who served as the Continental nominees upon the Halliwell Board from June of 1961 to the termination of the relationship between the two companies has been overwhelmingly established by the documentary record and testimony presented herein. It has likewise been established that, as a consequence of that domination and control, the initial contract of April 1, 1959 had become completely improvident and unfair by June of 1964.

Continental's insistence upon the continued enforcement of the 1959 contract by and through the subsequent contracts of 1964, 1967 and 1968, particularly since Continental completely directed and controlled Halliwell's performance of the 1959 contract since 1961, constituted an unconscionable abuse of Halliwell's rights and a gross violation of the defendants' fiduciary obligations in their control of Halliwell's assets and affairs.

Although the April, 1959 contract between Continental and Halliwell-Sedren may have been the product of an arm's length negotiation, *the subsequent contracts of 1964, 1967 and 1968 were exacted from Halliwell when it was dominated by Continental and unable to resist its demands.* Indeed, that control of Halliwell-Sedren commencing with June of 1961 enabled Continental to perpetuate and *enhance* the inequities of the 1959 agreement and enabled the defendants to exact monies and corporate opportuni-

ties from Halliwell which violated the most elementary standards of fair and equitable dealing.

Throughout the course of this action, the defendants have consistently claimed that, notwithstanding the election to the Halliwell-Sedren Boards of Directors of the individual defendants as nominees of Continental in 1961, and Continental's resulting absolute control of the Halliwell-Sedren assets and properties from and after 1961, they owed no fiduciary duties whatsoever to Halliwell-Sedren or its stockholders.

That thesis was approved by the Trial Court which explicitly held that the individual defendants, in serving as Halliwell Directors, "were acting as agents or servants of Continental by whom they were employed. Indeed, the record and depositions indicate that they were serving the interests of Continental in much the same as a majority of the Halliwell directors were seeking to serve the interests of Halliwell and Sedren" (49a-50a).* And, further, "The record indicates that much of the pressure asserted by Gordon on behalf of Continental had as its genesis Continental's desire to have Halliwell-Sedren live up to the 1959 contract". (51a)

As a result, the entire approach of the Trial Court to the resolution of the issues presented by the instant case was predicated upon the supposition that neither Continental nor the individual defendants owed any fiduciary obligation whatsoever to Halliwell-Sedren. Consequently, the Trial Court held that the activities of these defendants vis-à-vis Halliwell-Sedren, were perfectly legal because Continental was doing nothing more than "seeking to stand on its prior legal rights", and that, although those activities might have been "heavy handed", the is-

* The District Court ignored the fact that, at the April 12, 1967 meeting of the Halliwell Board which purported to approve the April 1967 contracts and releases to Continental, the Continental nominees were in fact a majority of the Halliwell directors.

sues of release and economic duress could only be considered as issues arising between two wholly independent parties, neither of whom owed any obligation of any kind to the other.

The argument of the defendants that they owed no obligations to the plaintiffs from and after their election as Halliwell directors in 1961, adopted in its entirety by the Trial Court, constitutes an incomprehensible repudiation of the most fundamental precepts of Anglo-American law which for decades have defined the duties and obligations of corporate directors.

It is elementary learning that a director is a fiduciary who undertakes, when he assumes his position upon a Board, an obligation of absolute fidelity to his *cestuis*, i.e. the Company and its stockholders. (*Lichtyger* v. *Franchard Corp.*, 18 N.Y. 2d 523, 539). The duties of a corporate director were formulated by the United States Supreme Court in *Pepper* v. *Litton*, 308 U.S. 295, 60 Sup. Ct. 238, as follows:

> "He who is in such a fiduciary position cannot serve himself first and his cestuis second. He cannot manipulate the affairs of his corporation to their detriment and in disregard of the standard of common decency and honesty. *He cannot by the intervention of a corporate entity violate the ancient precept against serving two masters.* He cannot by the use of the corporate device avail himself of privileges normally permitted outsiders in a race of creditors . . ."

No one compelled the Continental directors to become directors of Halliwell. Having done so, they were subject to every duty imposed by law upon every director of a corporation, no matter what their former or existing ties, relationships, loyalties or personal interests might be. They were *not* free to assert a prior and superior loyalty to Continental, in derogation of the interests of Halliwell. They were *not* free to utilize their positions upon the

Halliwell Board for the purpose of enforcing, enhancing or protecting a prior bargain no matter how unjust, disadvantageous or iniquitous that bargain was or had become during their tenure as directors. They were *not* free to prevent Halliwell from charting its own destiny predicated upon its own interests through directors who were not encumbered by other and superior loyalties and were therefore capable of exercising an unbiased judgment on behalf of Halliwell.

The Continental directors upon the Halliwell Board not only assumed their positions as Halliwell directors for the purpose of upholding and enhancing the interests of Continental under the 1959 contract; they were affirmatively dedicated to prevent any attempt by Halliwell to challenge, ameliorate or soften the harshness of its provisions and the consequences flowing therefrom, no matter how calamitous they had *become* to Halliwell.

In *Matter of Hubbell*, 302 N.Y. 246, Judge Fuld writing for a unanimous Court of Appeals, formulated the applicable principles which govern any situation involving the irreconcilable conflict between the self-interests of a fiduciary and his fiduciary responsibilities as follows (p. 259):

> "Under such circumstances, if an irreconcilable conflict between self-interest and fiduciary responsibility develops, *the choice of the trustee is either to subordinate the former or resign; 'thought of self was to be renounced, however hard the abnegation'. (Meinhard* v. *Salmon, supra*, 249 N.Y. 458, 468) As to the plaint that application of that principle results in unfairness to the husband, *let it be borne in mind that he voluntarily assumed his trusteeship. He was not obliged to become a trustee, 'but, as soon as he does so, he accepts whatever are the limitations, obligations and conditions attached to the position'. (Gratz* v. *Claughton*, 187 F. 2d 46, 49.)"

The obligation of loyalty which a director owes to his corporation and stockholders is indispensable to the "unprejudiced exercise of judgment" required of a director in discharging his duties. Courts will nullify any action of a Board "where the directors are guilty of misconduct equivalent to a breach of trust or *where they stand in a dual relation which prevents an unprejudiced exercise of judgment.*" (*Koral* v. *Savory Inc.*, 276 N.Y. 215, 216; *Geddes* v. *Anaconda Copper Mining Co.*, 254 U.S. 590).

The defendants do not even pretend that Gordon and the Continental directors exercised an unbiased and "unprejudiced" judgment on behalf of Halliwell in exacting the 1964, 1967 and 1968 contracts for the benefit of Continental. The Court below acknowledged in its opinion the total dedication of the Continental nominees to the interests of Continental and their total indifference to the interests of Halliwell. (49a-50a)

The liability of these defendants to the plaintiffs has been established by the decision of the New York Court of Appeals in *Chelrob Inc.* v. *Barrett*, 293 N.Y. 442, where the defendants, as distinguished from the defendants herein, made an honest and bona fide effort to discharge their fiduciary obligations as directors. In that case, the Court of Appeals held that a corporation dominated and controlled by another was entitled, as a matter of law, to recover the loss which had been sustained under an improvident contract approved by dual directors *even though those dual directors had sought to exercise an unbiased judgment in good faith relying upon the advice of experts.*

In that case, the Court was confronted with the relationship between the Long Island Lighting Co. ("Long Island"), the Queens Borough Gas and Electric Co. ("Queens") and the Nassau & Suffolk Lighting Co. ("Nassau"), all of which were public utilities organized in the State of New York. Long Island acquired control of both Queens and Nassau, although part of the cumulative preferred stock of both

Queens and Nassau remained in the hands of the public. Dominating both Queens and Nassau, Long Island fixed the price for gas purchased by Nassau from Queens.

An action was then brought by the preferred stockholders of Queens, contending that the price so fixed was unfair to Queens.

The Trial Court ruled that the price fixed by Long Island "was inadequate and caused loss to Queens" and granted a judgment in favor of Queens against Long Island and Nassau in the sum of $387,020 as an additional price for gas supplied after 1934. The Appellate Division for the Second Department then reversed the decision of the Trial Court, and directed a judgment dismissing the complaint upon the merits. The reversal was predicated upon the determination of the Appellate Division that the prices fixed by the directors controlled by Long Island had been determined, without fraud, in the exercise of their best judgment, and were therefore immune from attack, "even if it had been the result of bad judgment or error . . ." (p. 450).

The Court of Appeals agreed that the directors had acted in good faith and had neither sought nor obtained any personal benefit but nevertheless found that the rates fixed by them, although they "intended to exercise an unbiased judgment", were *unfair* and *improvident* so far as Queens was concerned. It thereupon reversed the Appellate Division and held that Long Island was responsible for the difference between the rate fixed and a fair rate to Queens.

The rules of law formulated and applied in the foregoing case were reaffirmed by the New York Court of Appeals in the case of *Ripley* v. *International Railways of Central America,* 8 N.Y. 2d 430. In that case, in sustaining a right of recovery, the Court found that "United (United Fruit Co.) was in practical control of Irca (International Railways of Central America). . . . and *stayed*

in a fiduciary relationship as respects the latter's minority shareholders insofar as concerned business transactions between Irca and United or its subsidiary."

The directors in the foregoing decisions, particularly in *Chelrob, Inc.*, made an attempt, albeit unsuccessfully, to deal fairly with their *cestuis*. The Continental nominees made none. They dealt with Halliwell as a captive to be bullied, threatened, badgered and squeezed. They completely flouted their directorial responsibilities to Halliwell as formulated by the New York Court of Appeals in the recent case of *Barr* v. *Wackman*, 36 N.Y. 2d 371, 380 that:

> "Directors undertake *affirmative duties of due care and diligence* to a corporation and its stockholders *in addition to* their obligation merely to avoid self-dealing. . . 'The personnel of a directorate may give confidence and attract custom; *it must also afford protection*'".

It is beyond dispute that a contract between a trustee and his *cestui* will be scrutinized by the courts with extraordinary care and jealous concern. (Perry, Trusts & Trustees, Vol. 2 (1929), §851, p. 1453). Much more than the considerations which would sustain the ordinary consensual engagement between strangers who are dealing at arm's length is required to validate a fiduciary's bargain with his beneficiary. The contract must be equitable and just. The trustee "takes the risk of an enforced surrender of his bargain if it turns out to be improvident" for his *cestui*. (*Globe Woolen Co.* v. *Utica Gas & Electric Co.*, 224 N.Y. 483). The fiduciary must discharge the burden of proving the fairness of the transaction. (*Geddes* v. *Anaconda Copper Co.*, 254 U.S. 590, 599). He must satisfy the conscience of the Court in every respect (*Sage* v. *Culver*, 147 N.Y. 241; *Irving Bank-Columbia Trust Co.* v. *Stoddard*, 292 Fed. 815, 819).

The defendants' utilization of the 1967 releases, obtained by their own vote, and the March 1968 termination agreement, exacted by the defendants from Halliwell under the desperate financial circumstances of Halliwell for which they themselves were responsible, constitutes an eloquent measure of the defendants' realization that they cannot be absolved of liability in any other way for the manner in which they debased their positions upon the Halliwell Board of Directors solely for the benefit of Continental.

POINT II

Releases, Ratification, "Settlement" Agreements and the Like Obtained by a Trustee From His Cestui Cannot Be Invoked to Exculpate the Trustee From His Breach of Fiduciary Duty Where the Cestui Has Not Been Fully Apprised of All the Facts as Well as the Legal Rights Which He Possessed.

A. Neither Continental Nor the Continental Nominees, Even If They Had Been Parties to the April, 1967 Releases or the March, 1968 Contract, Were Absolved by Those Documents From Their Violations of Their Fiduciary Obligations to Halliwell-Sedren

The agreement of March 15, 1968, purportedly approved by the Halliwell Board on April 8, 1968, was a contract exacted from Halliwell because of the appalling economic condition in which the defendants' depredations had left Halliwell. (Supra, pp. 39-43).

As appears from the record herein, Gordon minced no words. Either Halliwell complied with his demands, or Halliwell would be wiped out. The agreement of March 15, 1968, dictated by Gordon, was the price of survival. Halliwell had no choice but to surrender to the terms prescribed by Continental.

A release, waiver or settlement under far less onerous circumstances was recently considered by this Court in *Perlstein* v. *Scudder and German*, 429 F.2d 1136. In that case, this Court was confronted by an alleged settlement agreement and release of a cause of action in a securities fraud. In brushing aside the claimed "settlement" agreement and "release", the Court emphasized the fact that the settlement and release had been exacted from the plaintiff by the defendant because of the severe financial strain and pressures upon the plaintiff resulting from the defendant's violations of Regulation T.

In a recent decision, *Austin Instrument* v. *Loral Corp.*, 20 N.Y.2d 124, the New York Court of Appeals completely demolished every argument advanced by the defendants to avoid the consequences of its economic duress. Under circumstances involving no fiduciary obligations, the Court held that the plaintiff in that case had been compelled "to agree to an increase in price on the items in question under circumstances amounting to economic duress." It ruled that the evidence in that case—far less compelling than the evidence in this—"makes it a classic case, *as a matter of law*, of such duress".

The Court further dismissed all of the arguments which the defendants have advanced in this case to sustain the March 1968 agreement, including the argument (a) that Halliwell was free to enforce its remedies in a separate lawsuit which it could have instituted at the time; and (b) that Halliwell had waited too long to disaffirm the transaction.

The fact that the plaintiffs chose the lesser of the two evils with which it was confronted by Continental—surrender or extinction—does not mitigate or exclude the duress. As this Court pointed out in *First National Bank of Cincinnati* v. *Pepper*, supra, 633:

> "As Mr. Justice Holmes aptly observed 'It always is for the interests of a party under duress to choose the

lesser of two evils. *But the fact that a choice was made according to interest does not exclude duress'.*"

On April 8, 1968, the Halliwell Board purported to approve the March 15, 1968 agreement demanded by Gordon. By the third Whereas clause contained in that proposed contract with Continental, it was provided that "all of the aforesaid agreements and *releases* issued thereunder are hereby ratified, confirmed and approved in all respects . . .".

On April 8, the Board set May 13, 1968 as the date for the annual meeting of shareholders at which it was proposed to obtain the assent of the shareholders to the purported Continental-Halliwell termination agreement of March 15, 1968. *In the material sent to the shareholders, not a word appears therein which could possibly alert the shareholders to any of the facts reviewed in this brief* which bestowed upon Halliwell a right to recover from Continental for its depredations from June of 1964 to the date of the meeting.

None of the shareholders was advised that the 1964 and 1967 agreements and the releases delivered thereunder were absolutely void under existing law as well as Halliwell's By-Laws because they were unconscionable and had been procured by the vote of the Continental nominees themselves. None of them was informed of the manner in which Continental had appropriated to itself the corporate opportunities created by the diversion clause in the Nippon contracts and Continental's responsibilities to Halliwell therefor. None of them was furnished with a single fact which disclosed the defendants' violations of Halliwell's By-Laws or the breach of their fiduciary obligations to Halliwell and its stockholders which constitutes the gravamen of this action.

We are now told that, under such circumstances, the releases which the Continental nominees voted to Continental in 1967 were not only valid and subsisting when executed but were subsequently ratified by the stockholders

of Halliwell at its annual meeting of 1968. The argument is specious. In view of the fiduciary responsibilities which Gordon and the other Continental nominees owed to Halliwell and its stockholders, the defendants' claim herein that they have been absolved of their manifold breaches by the releases, the March 1968 agreement and stockholder ratification will not avail.

The care with which the Courts will examine a trustee's transaction with his *cestui* is intensified when the trustee contends that he is immune from any liability for a wrongful act because he had secured a release from the *cestui* or obtained the latter's ratification of the improper conduct. In that event, the trustee is not only bound to show that the *cestui* had been fully acquainted with all of the material and relevant facts; *he must, in addition, establish the beneficiary's knowledge of his legal rights, and 'how these facts would be dealt with by a court of equity.'* (*Adair* v. *Brimmer*, 74 N.Y. 539, 554; *Haviland* v. *Willets*, 141 N.Y. 35, 51).

The rationale of the foregoing doctrines was formulated by the Court of Appeals in *Adair* v. *Brimmer*, supra, at 553:

> "Confirmation and ratification imply to legal minds, knowledge of a defect in the act to be confirmed, and of the right to reject or ratify it. The cestui que trust must therefore not only have been acquainted with the facts, but apprised of the law, how these facts would be dealt with in a court of equity. All that is implied in the act of ratification when set up in equity by a trustee against his cestui que trust, must be proved, and will not be assumed."

That a Board of Directors may not refuse to compel restitution by one of its own members, or a former director, for the damages inflicted upon the Corporation by his fraudulent conduct, or grant him a release therefrom,

has been an unchallenged precept of corporate jurisprudence for generations. The conduct which it demands lies beyond the bounds of any discretion permitted to corporate directors. Claims of discretion, policy, expediency, or any of the thousand and one excuses which might be devised by an ingenious mind to justify a violation of its mandate, will not avail. Directors *must* compel restitution by a present or former director for the losses occasioned by his fraudulent conduct. A faithless trustee *must* account. Restitution *must* be enforced. Time and again the courts have been "petitioned to undermine the rule of undivided loyalty by the 'disintegrating erosion' of particular exceptions." (*Meinhard* v. *Salmon*, 249 N.Y. 458, 464). The standard has never been lowered by the judgment of any court known to us until this case.

"*A Board of Directors is without power to release one of their number from his liability to the Corporation* for the indirect misappropriation of its assets to his own use." (*Fletcher on Corporations*, Sec. 529). *Their attempt to do so may not even be ratified by a majority of the stockholders.** "The direct or indirect misappropriation of assets of the Corporation to his own use or benefit by an officer is incapable of being authorized or ratified by a vote on any act or omission of the majority of the stockholders." (*Pollitz* v. *Wabash, R.R. Co.*, 207 N.Y. 113, 127).

The case of *Gilbert* v. *Finch*, 72 App. Div. 38, affirmed in 173 N.Y. 455 is squarely in point. Dealing with a director's claim that he had been released from the breach of fiduciary obligations with which he was charged, the Court declared:

> "Nor do we think the board of directors or executive committee would have had the power, had they attempted to exercise it, to release Miller. By his act,

* The alleged ratification herein was effected by a vote of 3,637,875 shares out of 11,936,674 shares of Halliwell stock then outstanding, far less than a majority (Defts Ex. C, at 259A).

in connections with others, the property of the corporation had been wasted, and no act could have been done which would have released him or the others, except the restoration of the property to the corporation or it had been made good for the loss which it had sustained. If he could be relieved from liability in the manner claimed, then it is not difficult to see how each one of the defendants could also have been released in a similar way. Directors cannot waste the funds of a corporation which they represent, and then relieve themselves from liability by a release granted by themselves or their co-directors."

B. The Individual Defendants Who Are Not Parties to the April, 1967 Releases to Continental and the March 1968 Contract With Continental Cannot Claim That They Were Released by the Terms Thereof From Their Liability to the Plaintiffs for the Breach of Their Fiduciary Obligations as Directors of the Plaintiffs

The individual defendants' position herein is predicated upon the claim that they are the beneficiaries of the March 15, 1968 agreement between Continental and Halliwell-Sedren, *to which none of the individual defendants were parties*. That agreement purportedly constituted a ratification of the prior contracts between Continental and Halliwell-Sedren, *to which the individual defendants likewise were not parties*, as well as a ratification of the releases by Halliwell and Sedren to Continental executed in April of 1967, *running to Continental alone*. It is argued that these documents absolved *both Continental and the individual defendants* of any liability herein because the relationship between Continental and the individual defendants was that of master and servant. Consequently—so runs the argument—if Continental were absolved by the April 1967 releases of any responsibility to the plaintiffs because of its activities during the years that the individual defendants served as Halliwell-Sedron directors, it was absolved as the individual defendants' master

and *they, in turn, were likewise absolved as Continental's servants.*

To claim, as the individual defendants claim, that, as directors of Halliwell-Sedren, they were acting solely as *servants of Continental* is a startling affirmation of their inability to comprehend, let alone perform, their fiduciary duties to Halliwell Sedren during the many years that they served upon the Halliwell Board. They were not even aware of the fact that they were forbidden to serve two masters since they were only cognizant of one, Continental. Indeed, they insisted in their brief before Judge Owen upon their motion for summary judgment that they owed no fiduciary duties whatsoever to Halliwell-Sedren as Halliwell directors, a contention which they expressed in the following language:

> "The CCS nominees *bore no duty to Halliwell with respect to the 1959 contract* and there can be no subsequent breach of duty when the company's position with respect to that contract was *enhanced.*"

The foregoing words constitute an obvious affirmation of the fact that the individual defendants *utilized their positions as directors upon the Halliwell Board solely and only for the purpose of serving and enhancing interests of Continental, no matter how disastrous the consequences to Halliwell-Sedren.* As we have heretofore shown, supra pp. 48-55, the purported justification for their avowed disloyalty to the interests of Halliwell-Sedren, accepted by the Trial Court, constitutes a totally insupportable misstatement of existing law. (*Gilbert* v. *Finch*, 173 N.Y. 455, affirming 72 App. Div. 38)

The vice inherent in the individual defendants' arguments herein was underscored by the Court in *Rosenfeld* v. *Fairchild Engine & Airplane Corp.*, 201 Misc. 616, aff'd in 279 App. Div. 1086. In that case, the Board of Directors of the Fairchild corporation had released one Ward,

a former director, without an express reservation of its rights against Wilson or McComas, likewise former directors. The question presented was whether the corporation's release of Ward without an express reservation of its rights against Wilson and McComas discharged the latter from the liability asserted in the action brought by a stockholder on the corporation's behalf. It was argued in that case, as it is argued here, that "the corporation's release of Ward discharged Wilson and McComas from any liability to the corporation by reason of their acts or omissions as directors." In overruling that contention, the Court held at pp. 618, 620:

> "The question presented here is whether the corporation's release of Ward without an express reservation of its rights against the defendants Wilson or McComas, discharges the latter from the liability asserted in this action which purports to be brought on the corporation's behalf.
>
> * * *
>
> To hold that a board of directors could obtain immunity for themselves by releasing another director against whom the same charge of misapplication of funds is made would make a travesty of the law and of the responsibility of corporate directors. Such a conclusion would stultify the right of any stockholder to maintain a proceeding on behalf of his corporation and would further stultify the right and power of the court in passing upon the adequacy and fairness of the settlement of any such claim. If this is true, unscrupulous directors may circumvent the rules and checks which have been set up as a watch upon their activities."

CONCLUSION

In spite of every effort by the new Board of Halliwell and Sedren to rehabilitate those companies, the inordinate exactions by Continental took their final toll. In 1971, the operations at the Sedren mine were finally suspended. In 1975, the Government of Hati terminated the Sedren concession because of the non-payment of royalties and the suspension of operations. The Sedren mine never yielded eighty million pounds of copper despite eleven years of production. The present action represents the last and only hope of Sedren-Halliwell and their stockholders to recover the vast sums of which they were unlawfully deprived by the activities of these defendants.

For all the reasons and authorities hereinabove set forth, it is respectfully submitted that the judgment appealed from be reversed; that the defendants' defenses of release and settlement be dismissed; and that the case be remanded to the District Court or a Magistrate thereof for a computation of the damages sustained by the Plaintiffs (*Austin Instrument* v. *Loral Corp.*, 20 N.Y. 2d 124).

Respectfully submitted,

LOTTERMAN & O'CALLAGHAN
Attorneys for the Plaintiffs-Appellants
103 Park Avenue
New York, New York 10017
683-8281

Service of two (2) copies of the within Brief is hereby admitted this 3rd day of May, 1970

Sullivan & Cromwell

Attorneys for Defendants - Appellees
Continental Copper & Steel Industries, Inc.

Kay, Scarlett, Allen & Van Kleeck

Attorneys for Defendants - Appellees
Edward Hayes, Robert Hayes
and Joseph Steinhardt